

CALPINE CONSTRUCTION FINANCE COMPANY, L.P.

717 TEXAS AVENUE, SUITE 13.040
HOUSTON, TX 77002

VIA Federal Express and Electronic Mail

April 1, 2011

Mr. Charles Faust
Western Area Power Administration
114 Parkshore Drive
Folsom, CA 95630

SNR-FY12rateCase@wapa.gov

RE: WAPA Rate Order No. – 156

Dear Mr. Faust:

Pursuant to the January 3, 2011 Notice published in the Federal Register, Volume 76, No. 1, Calpine Construction Finance Company, L.P. ("Calpine") submits these comments on the 2012 proposed Central Valley Project ("CVP") transmission rates for the Western Area Power Administration – Sierra Nevada Region ("Western").

Summary:

Calpine believes that, as proposed, the modifications to Western's CVP rates, which will result in a more than 20 percent increase to Calpine, are unjust, unreasonable, and unduly discriminatory because the primary driver of the proposed rate increase is the construction of the Sacramento Voltage Support ("SVS") project, the need for which is attributable primarily to load growth in the greater Sacramento area and not to Calpine.¹

Calpine, on behalf of its Sutter Energy Center ("Sutter"), has not requested, was not consulted, and does not need or materially benefit from the construction of the SVS facilities, and yet would be burdened with a substantial and disproportionate share of the costs of those facilities. Indeed, Sutter's share of Western's total Transmission Revenue Requirement ("TRR") is approximately 22 percent.² As such, Sutter will bear 22 percent of the cost of the SVS project if Western's proposal is approved. However, the benefits of the SVS project will

¹ Press release of April 29, 2008 from Western titled "Sacramento Area Voltage Support Decision Issued" ("The need for the transmission reliability in the Sacramento area is ongoing. Growth in the greater Sacramento area has increased the demand on the interconnected electric system leading to transmission system overloads.").

² 2012 Rates Brochure: Proposed Rates for Power, Transmission and Ancillary Services ("Rates Brochure"), dated January, 2011. Appendix C, page 2. Sutter's transmission is 500 MW of an average CVP use of 2,225 MW.

accrue predominantly to localized load in the Sacramento area rather than to Sutter, which is an independent electric generation facility that is dynamically scheduled into the CAISO operated markets.

In lieu of the current proposal, Calpine requests that Western determine the expected beneficiaries of the SVS project and allocate costs roughly in proportion to the benefits those beneficiaries will receive. FERC is now requiring this approach and, as an entity with a reciprocity tariff approved by FERC, Western should do so as well. In addition, for the reasons discussed below, the proposed rates should reflect Western's sale of 270 MW of incremental capacity following the completion of the SVS project.

Finally, as discussed below, this rate increase, when combined with the lack of market opportunity or compensation for reliability services has forced Sutter to seek a direct connection with the CAISO and possibly terminate its contractual relationships with Western. Western has and Sutter believes that Western should continue to work cooperatively with Calpine to facilitate Sutter's departure from the Western Sub-Balancing Authority ("SBA").

Background on Sutter

Sutter is a nominal 542 MW combined cycle facility located outside of Yuba City in Northern California. The facility is a combined cycle configuration of two Siemens FD1 combustion turbines, two Vogt heat recovery steam generators, and a Siemens Westinghouse steam turbine generator. Sutter commenced operation on July, 2001, when Western's transmission facilities were integrated in, and a part of the California Independent System Operator ("CAISO"). This integration was effected, in large part, through Contract 2948A with PG&E.

The facility is interconnected to Western's 230 kV system via a 3.5 mile generation tie-line to the O'Banion substation. While the facility is located in the Western Sub-Balancing Authority ("SBA"), pursuant to arrangements with both Western and the CAISO, the facility is operated as part of the CAISO balancing authority area and Sutter's output is dynamically scheduled through a pseudo-tie arrangement into the CAISO operated markets. Sutter's transmission rights on WAPA's system are limited to 500 MW of Network Integration Transmission Service ("NITS") to effectuate the pseudo-tie arrangement. Service under the NITS agreement is conditioned on there being in effect a remedial action scheme, as set forth in the Interconnection Agreement between Calpine and Western, to protect Western's power system.

Sutter was built in a "soft spot" on the transmission grid and, in addition to providing energy and capacity for the last 10 years, has provided needed voltage support for the Sacramento Region. Western initially compensated Sutter for its

provision of reactive power but discontinued such payments in late 2006 pursuant to FERC's comparability policy for reactive power compensation. Sutter finds this action particularly relevant and egregious given that the SVS project is apparently designed to replace the reliability value of Sutter and now Sutter is asked to pay for a significant share of SVS.

As a result of the financial burdens of having to procure transmission from Western in order to reach CAISO markets, coupled with Western's refusal to compensate Sutter for its reliability services (e.g., reactive power) and the absence of any market demand in the Western SBA or Sacramento Municipal Utility District ("SMUD") BA, Sutter is seeking a new interconnection directly with CAISO-controlled grid facilities.

Cost-drivers for the Western Rate Increase

Calpine understands that there are two primary factors driving the proposed rate increase, a cost-of-service study which newly allocates facility costs between transmission and non-transmission functions, and the inclusion of new capital replacements and additions.

The cost-of-service study substantially increases the allocation of costs to the transmission function when compared with non-transmission functions. This shift in total allocation is driven by the substantial cost of the SVS, and less-substantially driven by changes in the functional designation of other facilities. Indeed, the 2012 CVP cost-of-service study allocates 59.54 percent of the \$63.7 million, Total Revenue Requirement ("TRR") of CVP transmission, or \$37.3 million to the transmission function, and therefore to transmission rates including NITS³. Current rates include a much lower transmission-function allocation percentage yielding a transmission-allocated revenue requirement of only \$28.8 million.

The proposed 2012 increase in revenue requirement of \$8.5 million is almost entirely explained by the inclusion of SVS in transmission rates. Indeed, through data responses, Calpine has discovered that the direct incremental revenue requirement for the SVS for 2012 is estimated at \$6.6 million⁴. Additionally, if one were to include the indirect allocation effects related to the inclusion of the SVS project into rates⁵, it may entirely explain the increase. Stuningly, the SVS project represents an addition of an estimated \$57.4 million⁶

³ Rates Brochure, Table VIII – 1 on page 58

⁴ See Attachment 1, "Selected SNR Responses to Data Requests", CPN-10

⁵ The indirect cost allocation is described at page 57 and 58 of the Rates Brochure. The inclusion of SVS in the transmission plant appears to greatly affect the allocation factor.

⁶ Attachment 1, CPN-19

to a pre-existing, net-transmission-plant total of \$83.5 million⁷. SVS therefore represents an increase in net transmission plant of over 68 percent.

The SVS project apparently adds incremental transfer capability into Sacramento, particularly to the area of explosive load growth served by the SMUD around the Natomas substation⁸. In a data response, Western indicated that it has executed a contract to sell up to 270 MW across an unidentified path contingent upon completion of the SVS.

"Western executed a contract in May 2008 with up to 270 MW capacity contingent upon adding Network Transmission facilities and upgrades including the construction of the O'Banion-Elverta and O'Banion-Natomas 230kV Transmission Lines that may create ATC on the requested path, which is already obligated under contract⁹."

However, from a ratemaking perspective, Western only included an incremental 126 MW of incremental transfer capacity (less than half of that negotiated in the "contingent" contract) in its rate calculations¹⁰. If one were to allocate the full transmission revenue requirement of the SVS to this incremental transfer capability, the price would be approximately \$4.36 per kW-month,¹¹ or exactly 4 times the current CVP PTP rate of \$1.08 per kW-month.

Western states that uncertainty in transfer capability will be resolved only after the project is completed when "cost and available transmission"¹² can be determined. Calpine cannot determine what uncertainty remains, given that the project is very near completion. Nonetheless, if Western had included the full 270 MW in rates (without any change to the methodology of the Rates Brochure), Calpine estimates that the PTP rate would be reduced from the proposed \$1.32 per kW-month to \$1.245 per kW-month.¹³

Sutter Derives no Commensurate Benefits from Western's SVS Investment

Western offers no showing to demonstrate that customers such as Calpine will receive any benefit from the SVS project. Through discovery, Calpine sought an explanation of the presumed benefits that might be derived by Sutter from the SVS project. Western did not identify any specific attributes of SVS that would benefit to Sutter. Rather, Western claims that:

⁷ FY 2008 value as reported at p7 of Western's Cost-of-Service Overview presentation, April 23, 2009.

⁸ Attachment 1, CPN-20

⁹ Attachment 1, CPN-9

¹⁰ Rates Brochure, page 61

¹¹ 6.6 million /126/12/1000

¹² Attachment 1, CPN-15

¹³ Attachment 2 contains the calculations supporting this estimate.

Western is constructing the SVS facilities for the continued reliable operations of Western's transmission system, and as a result, all of Western's transmission customers receive benefits.¹⁴

Calpine respectfully disagrees with this conclusory and unsubstantiated statement. Indeed, not all of Western's customers benefit, and they certainly do not all benefit equally, as rolled-in ratemaking would suggest. Calpine specifically sees no direct benefit. As noted above, Calpine's NITS is conditioned on maintaining its interconnection agreement, which includes a remedial action scheme specifically designed to protect Western's system. Any changes to the remedial action scheme following the completion of the SVS project are expected to be inconsequential to Sutter's operation. Thus, Calpine is neither the proximate cause for nor a meaningful beneficiary of the reliability upgrade occasioned by the SVS project. Yet, Western asks that Calpine fund 22 percent of the cost of the project.

Moreover, Western's assumption that all customers will benefit from the network upgrade is inconsistent with FERC's evolving cost allocation policy. While all customers may benefit to some degree from a network expansion, rolled-in pricing is appropriate only when all customers benefit to approximately the same degree as the costs they are allocated.¹⁵ On June 17, 2010, FERC issued a Notice of Proposed Rulemaking on transmission planning and cost allocation in which it proposed new cost allocation principles, which would preclude any allocation to customers that receive no benefit and require that costs be allocated to those that do benefit in a manner that is roughly commensurate with estimated benefits.¹⁶ Consistent with the Transmission NOPR, FERC has approved proposals submitted by the Southwest Power Pool ("SPP") and the Midwest Independent Transmission System Operator ("MISO") to allocate the costs of transmission facilities on a rolled-in basis, using the same "roughly commensurate" standard.¹⁷ Notably, both SPP and MISO presented tangible and qualitative benefits to demonstrate real and substantial benefits to justify their proposed rolled-in pricing. As Western also may be aware, there are proposals pending in Congress (e.g. the Corker amendment) to further amend

¹⁴ Attachment 1, CPN-16

¹⁵ See *Illinois Commerce Commission v. Federal Energy Regulatory Commission, et al.*, 576 F.3d 470 (2010) (remanding FERC's decision to allocate the cost of new transmission facilities in PJM on a rolled-in basis, holding that, while there would no doubt be some benefit to all customers FERC had failed to establish that the benefit was enough to justify the costs being allocated).

¹⁶ *Transmission Planning and Cost Allocation by Transmission Owning and Operating Public Utilities*, 131 FERC ¶ 61,253 (2010) ("Transmission NOPR").

¹⁷ *Southwest Power Pool, Inc.*, 131 FERC ¶ 61,252 (2010) ("SPP"); *Midwest Independent Transmission System Operator, Inc.*, 133 FERC ¶ 61,221 at P 192 (2010) (noting that while the Transmission NOPR has not been finalized, "the Commission remains mindful of its goals in evaluating the Filing Parties' proposal").

the Federal Power Act to require a cost allocation "reasonably proportionate to measurable economic and reliability benefits."

Thus, both FERC and Congress are moving away from the assumption that all transmission customers benefit equally from any addition to the transmission system, and in favor of a more exacting review of who benefits from the transmission additions and a cost allocation that is at least roughly commensurate with the prefatory determination of benefits. Accordingly, Western should identify the primary beneficiaries of the SVS project and, based on the results of that analysis, propose an alternative cost allocation consistent with FERC's current policy.

Western's tariff grants it discretion to allocate the costs of new transmission upgrades based on demonstrable benefits. Specifically, Attachment P, Part II, Section 5.1 of Western's FERC-adopted OATT states: "Western will utilize a case-by-case approach to allocate the costs of new transmission projects." Part I of the same Attachment P further recognizes the principles of cost causation and benefit in determining participation in, and funding of, transmission upgrades. Indeed, since FERC now requires that costs be allocated roughly in proportion to benefits, Western may be required to do so under its reciprocity tariff approved by FERC.

Recommended Alternatives to Western's Proposal

Calpine has compiled alternatives to Western's primary proposal. The following recommendations are not mutually exclusive. Calpine believes that these proposals result in a more just and reasonable resolution than the initial proposal of Western.

(1) Include All Transfer Capacity in Rates Calculation

As noted above, Western has included only about half of its projection of the incremental PTP capacity provided by the SVS project. This is inconsistent with the fact that Western has apparently entered into a contract to sell, albeit conditionally, the full 270 MW of transfer capacity. While we are encouraged by Western's apparent willingness to revisit this "when the project is complete,"¹⁸ Western's review may be too late to include this valuable capacity in 2012 rates.

The failure to include the total incremental capacity in rates will result in an inter-generational shift of cost recovery. That is, current transmission customers will be paying a higher rate and later transmission customers (at the latest, post 2016) would receive the

¹⁸ Attachment 1, CPN-15

benefit of a possible over-collection. Calpine cannot predict the timing or success of its departure from the Western SBA, but it is certainly conceivable that Sutter may not receive the benefit of over-collection-related rate reductions in the future.

(2) Use Reasonable Discretion to Propose Alternative Designs

As indicated above, Western has the ability to allocate the costs of new transmission on a case-by-case basis. At this point, Western appears to have ignored the specific facts of this project which might suggest that this case requires a unique solution.

First, the cost of the SVS *significantly increases* the total net transmission plant recovered in rates. In no definition is this a small or insignificant project that can be rolled in without significant impact on Transmission Customers.

Second, the benefits of the SVS project are not commensurate with the costs to Sutter. Sutter derives no specific benefit from the SVS project, has not requested it be built, and the alleged voltage support benefits of the project accrue to others.

Indeed, not only does Western continue to refuse to pay Sutter for the reactive power service it has provided to the SBA and Region for 10 years, now it seeks to *charge* Sutter for what appears to be a transmission solution to voltage support provided by Sutter. Calpine requests clarification of the extent to which the transmission upgrade will reduce or eliminate the need for Western to rely on Sutter for voltage support.

Finally, Western should consider reinstating compensation to generators, including Sutter, for reactive power supplied to support the Sacramento Region, particularly to the SMUD and Roseville service areas.

Charles Faust
April 1, 2011
Page 8

If you have any questions regarding the foregoing, you may contact me at (925) 557-2231.

Respectfully submitted,

Calpine Construction Finance Company, L.P.

A handwritten signature in black ink, appearing to read "Mark J. Smith", with a long horizontal flourish extending to the right.

Mark J Smith
Vice President, Market Design
Calpine Corporation

Attachment 1, Page 1 of 2

Selected SNR Responses to Data Requests

CPN-9

Has Western executed contracts for the incremental 126 MW of PTP capacity created by SVS?

Western executed a contract in May 2008 with up to 270 MW capacity contingent upon adding Network Transmission facilities and upgrades including the construction of the O'Banion-Elverta and O'Banion-Natomas 230kV Transmission Lines that may create ATC on the requested path, which is already obligated under contract. For 2012 rate forecasting purposes, Western forecasted 126 MW of transmission capacity sales due to the additional network capacity.

CPN-10

Please provide the incremental revenue requirement incurred solely as a result of the SVS project. Please include O&M, depreciation and interest expense.

The estimated 2012 increase in the Transmission Revenue Requirement due to SVS is as follows (Facility Value: \$57.4 million assumed completion in April 2011):

O&M Expense:	\$5.3	million
Depreciation Expense:	\$1.0	million
Interest Expense:	\$0.3	million
Total:	\$6.6	million

CPN-15

In CPN-9, Western states that it signed a contract for 270 MW of capacity, but only included an incremental 126 MW in the rate calculation. Why?

Western executed a contract for up to 270 MW capacity. At the time of the rate forecast, Western estimated its cost and related transmission available for sale. Actual cost and available transmission will be determined when the project is completed and Western determines the amount of transmission that is available for sale up to 270 MW.

CPN-16

Please generally identify the specific benefits that Calpine/Sutter will receive as a result of the SVS project.

The SVS project supports Western's bulk electric system and improves reliability. Western is constructing the SVS facilities for the continued reliable operations of Western's transmission system, and as a result, all of Western's transmission customers receive benefits.

Attachment 1, Page 2 of 2

Selected SNR Responses to Data Requests

CPN-19

Of the total transmission plant from above, what was the assumed value of SVS transmission plant?

Western's estimated SVS plant value included in transmission plant above is \$57.4 million.

CPN-20

Does Western serve retail load in or near the Natomas substation? If not, please identify the party or parties that serve retail load from any distribution or transmission circuits terminating at Natomas.

Western does not serve retail load. Western serves wholesale and federal end use customers at various points of interconnection. SMUD is the retail service provider in the area of the Natomas substation.

Attachment 2

Calpine's Alternative Calculation of PTP costs

CVP Rate Calculation and Proposed Revision			
	Item	Amount	Source
1	Total Allocated CVP Transmission Revenue Requirement	\$37,284,455.00	Rates Brochure, P 58
2	Western Proposed PTP Calculation		
3	Long-term Contracts	659	Rates Brochure, P 59
4	NITS	<u>1,692</u>	Rates Brochure, P 59
5	TOTAL	2,351	Rates Brochure, P 59
6	Proposed PTP Rate (\$/kW-Mo)	\$ 1.32	Line 1/Line 5/1000/12
7	Calpine Proposed PTP Calculation		
8	Long-term Contracts	803	Add (270 - 126) to Line 3
9	NITS	<u>1,692</u>	Rates Brochure, P 59
10	TOTAL	2,495	Line 8 plus Line 9
11		\$ 1.25	Line 1/Line 10/1000/12